

Message Text

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TO AMEMBASSY NEW DELHI

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SUBJECT: TAX EXEMPTION FOR AIRLINES

REF: NEW DELHI 1242

1. AN EXCHANGE OF NOTES GRANTING A RECIPROCAL TAX EXEMPTION FOR AIRLINES CANNOT BE LIMITED ONLY TO CORPORATIONS. THE UNITED STATES INTERNAL REVENUE CODE, SECTION 883(A) (2) PROVIDES THAT THE EARNINGS OF A FOREIGN CORPORATION DERIVED FROM THE OPERATION OF AIRCRAFT WILL BE EXEMPTED FROM U.S. TAXATION ONLY IF THE AIRCRAFT IS REGISTERED UNDER THE LAWS OF A FOREIGN COUNTRY QUOTE WHICH GRANTS AN EQUIVALENT EXEMPTION TO CITIZENS OF THE UNITED STATES AND TO CORPORATIONS ORGANIZED IN THE UNITED STATES UNQUOTE. SINCE THE STATUTE PROVIDES A U.S. TAX EXEMPTION ONLY WHERE THE FOREIGN COUNTRY GRANTS AN EQUIVALENT EXEMPTION TO BOTH

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U.S. CITIZENS AND CORPORATIONS, AN AGREEMENT FOR A

RECIPROCAL AIRLINE TAX EXEMPTION LIMITED ONLY TO CORPORATIONS WOULD REPRESENT A MODIFICATION OF U.S. LAW REQUIRING A FORMAL TREATY RATIFIED BY THE SENATE. FYI AND WITH REFERENCE TO THE REASONS GIVEN BY THE INDIANS FOR LIMITING THE AGREEMENT TO CORPORATIONS, WE NOTE THAT IF NO INDIVIDUALS ARE PRESENTLY ENGAGED IN THE AIRLINE BUSINESS AND NONE ARE LIKELY TO BE SO ENGAGED IN THE FORESEEABLE FUTURE, THEN, AS A PRACTICAL MATTER, A RECIPROCAL AGREEMENT EXTENDING TO U.S. AND INDIAN CITIZENS SHOULD POSE NO PROBLEMS FOR THE GOI. END FYI.

3. THE AGREEMENT MAY BE EFFECTIVE AS OF JANUARY 1, 1976, REPEAT 1976, IF THE FORMAL PROCEDURES ESTABLISHING THE AGREEMENT ARE COMPLETED BY THE END OF 1976. FYI AS A MATTER OF POLICY, WE ARE RELUCTANT TO EXTEND THE DATE FOR RETROACTIVE EFFECT OF AN AIRLINE TAX EXEMPTION AGREEMENT BEYOND THE BEGINNING OF THE YEAR IN WHICH THE AGREEMENT IS CONCLUDED. END FYI.

4. FYI AND WITH REFERENCE TO THE INDIAN REDRAFT OF THE U.S. NOTE, WE OBSERVE THAT, IN ADDITION TO LIMITING THE AGREEMENT TO CORPORATIONS, THE REDRAFT CONTAINS A DEFINITION OF THE TERM "OPERATION OF AIRCRAFT" AND PROVIDES FOR SPECIFIC EXTENSION OF THE AGREEMENT TO PARTICIPATION IN AIR TRANSPORT POOLS OF ANY KIND. WE PREFER DELETION OF THESE ADDITIONAL ITEMS AND WOULD REPROPOSE THE TEXT OF OUR ORIGINAL DRAFT FOR THE FOLLOWING REASONS:

A. THE DEFINITION OF THE TERM "OPERATION OF AIRCRAFT" IS ONE WHICH IS GENERALLY UNDERSTOOD IN COMMERCIAL PRACTICE AND, HENCE IS REALLY UNNECESSARY IN THE AGREEMENT. MOREOVER, ON ITS FACE, THIS DEFINITION WOULD CREATE AN APPARENT INTERNAL INCONSISTENCY IN THE AGREEMENT BECAUSE IT DOES NOT INCLUDE INCOME FROM THE INCIDENTAL LEASE OF AIRCRAFT WHICH IS OTHERWISE EXEMPTED.

B. WE DO NOT UNDERSTAND WHAT IS MEANT BY A "PARTICIPATION IN A POOL OF ANY KIND REGARDING AIR TRANSPORT," AND ACCORDINGLY ARE UNCERTAIN LIMITED OFFICIAL USE

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WHETHER SUCH A PROVISION WOULD EXTEND THE AIRCRAFT TAX EXEMPTION BEYOND THE PERMISSIBLE LIMITS OF U.S. LAW. FURTHER, TO THE EXTENT THAT INCOME DERIVED FROM PARTICIPATION IN SUCH POOLS WOULD OTHERWISE BE EXEMPT UNDER THE GENERAL PRINCIPLES EMBODIED IN THE AGREEMENT, SUCH A PROVISION AGAIN APPEARS UNNECESSARY. END FYI.

5. FINALLY, THE EMBASSY IS REQUESTED TO DETERMINE THE
PRESENT STATUS OF FORMAL INCOME TAX TREATY NEGOTIATIONS
TENTATIVELY SCHEDULED AT OUR OCTOBER 1975 MEETING FOR
THE SPRING OF 1976.
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